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Special Steps Needed for Paper 1040 Filers to Claim Late Tax Changes

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Following the enactment of late tax legislation in December, taxpayers using a paper Form 1040 will need to follow special instructions if they are claiming any of three key deductions.

The late changes affect a number of areas of tax law, but the most significant effect on taxpayers involves the state and local sales tax, higher education tuition and fees, and educator expenses.

The major forms for the filing season (Forms 1040, 1040A, Schedule A&B, and instructions) went to print in early November and reflect the law in effect at that time. The instructions contain a cautionary note to taxpayers that the legislation was pending at the time of printing. Even though these forms were printed before the law changed, the IRS emphasized that taxpayers should use the current Form 1040 or file electronically to claim the three key "extenders" deductions.

However, the IRS will not be able to process tax returns claiming these three deductions until early February because updates are being made to tax processing systems. Neither paper nor electronic tax returns claiming these deductions should be filed during this period.

When processing begins for these deductions, the IRS encourages taxpayers to file electronically, which will reduce the chance for making errors on these new provisions.

For those filing a paper 1040, there are special steps they will need to follow to claim the deductions:

State and Local General Sales Tax Deduction:

- The deduction for state and local general sales taxes will be claimed on Schedule A (Form 1040), line 5, "State and local income taxes." Enter "ST" on the dotted line to the left of line 5 to indicate you are claiming the general sales tax deduction instead of the deduction for state and local income tax.
- The IRS also will issue Publication 600 for 2006, which includes the state and local sales tax tables, a worksheet and instructions for figuring the deduction.

- This option is available to all taxpayers regardless of where they live, though it's primarily designed to benefit residents of the eight states without state and local income taxes.

Higher Education Tuition and Fees Deduction:

- Taxpayers must file Form 1040 to take this deduction for up to \$4,000 of tuition and fees paid to a post-secondary institution. It cannot be claimed on Form 1040A.
- The deduction for tuition and fees will be claimed on Form 1040, line 35, "Domestic production activities deduction." Enter "T" in the blank space to the left of that line entry if claiming the tuition and fees deduction, or "B" if claiming both a deduction for domestic production activities and the deduction for tuition and fees. For those entering "B," taxpayers must attach a breakdown showing the amounts claimed for each deduction.

Educator Expense Adjustment to Income:

- Educators must file Form 1040 in order to take the deduction for up to \$250 of out-of-pocket classroom expenses. It cannot be claimed on Form 1040A.
- The deduction for educator expenses will be claimed on Form 1040, line 23, "Archer MSA Deduction." Enter "E" on the dotted line to the left of that line entry if claiming educator expenses, or "B" if claiming both an Archer MSA deduction and the deduction for educator expenses on Form 1040. If entering "B," taxpayers must attach a breakdown showing the amounts claimed for each deduction.